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MARR, MASS, TT

SUBJECT: TIMOR-LESTE AT TEN YEARS: TO THE BRINK AND BACK

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11. (SBU) SUMMARY: Ten years after the August 30, 1999, referendum that put it on the road to formal independence, Timor-Leste remains an underdeveloped ward of the international community. Early efforts to portray the country as a triumph of international nation-building were shattered by violent chaos in 2006 as personal, institutional, geographic and generational rivalries exploded to the surface, leading to a frantic call for the return of international security forces to keep order. Basic governance institutions still lack essential capacity and enjoy uncertain popular credibility, and an over-reliance on foreign experts in some cases may actually have impeded their development. As it celebrates ten years free of hostile foreign occupation Timor-Leste is enjoying eighteen uninterrupted months of relative calm, the longest such stretch in its history, raising hopes that it may have at last turned a corner toward sustained stability and development. To avoid continued disappointment in the years ahead, Timor-Leste must dramatically improve the capacity of its institutions across the board; effectively harness its petroleum revenue to build its economy and encourage its private sector; and peacefully usher in a new generation of political leaders. The United States has a unique role to play in promoting economic development and reform of the security and justice sectors so that our interest in making Timor-Leste a more stable and prosperous democracy is achieved. END SUMMARY.

12. (SBU) Timor-Leste in 1999 had no history of governing itself. A 24-year Indonesian occupation, which is estimated to have caused well over 100,000 deaths, followed three centuries of Portuguese colonization. Indonesia's scorched earth departure destroyed approximately 80 percent of Timor's economic infrastructure (utilities, public buildings, houses) and left Timor-Leste without a professional class experienced in governing. In retrospect, justified enthusiasm for the cause of Timorese independence obscured the enormous challenge of launching a new country basically from scratch.

Security Threat Proves to Be Internal

¶3. (SBU) The post-referendum violence and destruction, and the presence of hostile militia elements across an ill-defined border with Indonesian West Timor, raised initial fears that Timor-Leste would face immediate external security threats, but such fears were not realized. Vigorous early work on border demarcation during the 1999-2002 transition period reduced the number of potential flashpoints. Critically, domestic politics evolved in both Timor-Leste and Indonesia to create an atmosphere conducive to reconciliation, as Indonesia redefined itself in the post-Suharto era and Timor-Leste acknowledged the unavoidable imperative of repairing relations with its much larger neighbor. The positive state of bilateral relations between Timor-Leste and Indonesia today is a considerable accomplishment in which both sides can justifiably take great pride. Representative of the current warm state of bilateral relations, Timor-Leste recently invited the commander of Indonesia's armed forces to visit. Likely to take place in September 2009, the Indonesian general's sojourn to Dili would be the first since the events of 1999.

¶4. (SBU) The greatest threat to Timorese security proved to be internal. As the UN presence drew down after formal

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independence in May 2002, old domestic rivalries buffeted fragile institutions that were ill-equipped to manage conflict peacefully. A combination of factors -- personal animosity among political elites; institutional tensions both within the military and between the military (drawn heavily from the independence-era guerrilla force) and the police (populated in part with Indonesian holdovers); regional jealousies (Westerners alleging bias in favor of the East); and generational grievances by the younger Timorese who felt their contributions to the independence struggle had not been sufficiently recognized -- joined together to produce the crisis of 2006. Two months of street violence claimed dozens of lives, brought down the Alkatiri government, resulted in widespread property destruction and 150,000 internally displaced persons (IDPs) and took the country to the brink of an anarchic civil war. As in 1999, order was restored by an international security force led by Australia, eventually supplemented with a renewed United Nations peacekeeping mandate that continues today. The 2006 crisis was Timor's most serious test as an independent country, one that it failed miserably.

Economy: Real Development Lagging Behind

¶5. (SBU) As it did ten years ago, Timor-Leste ranks among the least developed economies in the world. Non-oil per capita gross domestic product of \$350 places it toward the bottom of the rankings of low income countries. The economy is split into two very unequal parts -- the 85 percent of the work force devoted to subsistence agriculture (cooking with firewood and fetching water), alongside a services sector (60 percent of the economy by value, an extremely high level for an LDC) driven by

the needs of the large international presence in the country as well as spiraling government spending. Timor's nominal wealth began to increase in 2005 when revenue from a gas field shared with Australia began to come online. The increased income went overwhelmingly to purchasing imported goods and cash pay-outs to resolve the political problems of IDPs and pensioners, however, leaving domestic production little changed and poverty levels actually worse than ten years ago. The UN ranks Timor-Leste 158th of 179 countries in terms of human development indicators. Petroleum revenue has boosted nominal statistics like gross national income, making Timor-Leste look more prosperous on paper, but that stimulative demand effect has yet to filter into the real domestic economy.

¶6. (SBU) Two of Timor-Leste's biggest economic decisions -- to set up a special petroleum fund to manage its revenue on a sustainable basis and to dollarize the economy -- remain two of its best. By smoothing petroleum income and removing the possibility of exchange rate appreciation Timor-Leste has avoided the worst of the Dutch Disease that often plagues resource-rich economies. On the negative side, Timor's private sector remains extremely small. A major obstacle is the poor regulatory environment for business, which the World Bank ranks 170th of 181 countries. The country's infrastructure needs, from schools to roads, water and power, are immense. Half of the adult population has zero educational attainment and functional illiteracy and innumeracy are well above 70 percent.

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Accountability and Impunity

¶7. (SBU) Despite the suffering that took place in 1975-99, the desire to hold Indonesia accountable for the crimes committed during its occupation is not a pressing issue for most Timorese. Timor-Leste views itself as the victorious party, having won its independence. Two reports catalog the events of the Indonesian occupation and departure. The Commission for Reception, Truth and Conciliation (CAVR) submitted the Chega! (Enough!) report to the Timorese parliament in 2005, describing the 1975-99 period. The bilateral Indonesia-Timor-Leste Truth and Friendship Commission in its June 2008 report assigned institutional responsibility for 1999 human rights violations to the Indonesian military. Both reports have been submitted formally to the parliament but neither has been publicly debated. Documenting the evidence preserves the possibility of justice in the future, but the Timorese leadership has no intention of pursuing Indonesian accountability now.

¶8. (SBU) Timor-Leste has domestic accountability issues as well. A UN Commission of Inquiry documented possible illegal actions from the 2006 petitioners crisis. Some criminal cases have moved forward but the president has repeatedly proposed a general amnesty for 2006 crimes. A group that includes former petitioners is on trial for the 2008 attacks against the president and prime minister, but the president indicated he may pardon them if convicted. The reluctance to hold guilty parties accountable for their crimes demonstrates a lack of faith that Timorese society could hold together if stressed and creates a culture of impunity that threatens to undermine the rule of law and perpetuate the violent political environment that has plagued the country.

The Challenges of Timor's Next Ten Years

¶9. (SBU) Timor-Leste is a long-term project with decades of work left undone. For the first time in its history it has its political independence and a moderate amount of domestic economic resources. Without continued support, the right decisions and great determination, however, Timor-Leste could still fail. Timor-Leste's success over the next ten year period will be shaped by its response to several key challenges.

Ensuring an Appropriate Draw Down of UN Presence and ISF

¶10. (SBU) On three occasions, in 1975, 1999 and 2002, Timor-Leste has been ill-prepared for full sovereignty. The timing of the fourth opportunity must be driven by a clear analysis of the conditions on the ground as well as the capability of Timor-Leste's governance institutions. The security sector is the biggest and most obvious test. The

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International Stabilization Force (ISF) reduced its numbers by 20 percent earlier this year and appears poised to consider further reductions in the near future. UN police this year have ceded primary law enforcement responsibility back to Timorese police in three of 13 districts. In both instances the drawdowns are in response to improving security conditions and fledgling improvements in local capacity.

Ushering in the Next Political Generation

¶11. (SBU) Timor-Leste's political history to date has been dominated by three figures: Prime Minister Xanana Gusmao, President Jose Ramos-Horta, and Fretilin Secretary General and former PM Mari Alkatiri. These three elder statesmen (Gusmao is 63 years old; Alkatiri and Ramos-Horta will both turn 60 later this year) represent the generation that remembers the Portuguese colonial era. Over the course of the next two election cycles, due in 2012 and 2017, they will likely be confronted with a new generation of voters and leaders. No figure on the horizon, however, has Gusmao's profile at home or Ramos-Horta's abroad.

¶12. (SBU) While there are many with aspirations for the country's highest political positions, including the incoming Ambassador to the U.S. Constancio Pinto, four individuals are likely to be involved in the next round of jockeying for the two senior leadership positions of president and prime minister.

-- Taur Matan Ruak, Commander of the Armed Forces (53 years

old). TMR was a guerrilla colleague of Gusmao's during the Indonesian occupation. He was a central player in the 2006 crisis and was recommended for prosecution by the UN Commission of Inquiry. Nevertheless, he is seen and occasionally revered as a founder of the nation due to his long service in the military resistance. Gusmao's CNRT party could support TMR as a presidential candidate.

-- Fernando "Lasama" de Araujo, President of Parliament (46 years old). Lasama founded the Democratic Party (PD) and led it into the parliament as Fretilin's first opposition. He served as interim President of the Republic after Ramos-Horta was shot in 2008. With Ramos-Horta uncertain to stand again for the presidency, Lasama is a leading candidate to replace him.

-- Jose Luis Guterres, Deputy Prime Minister and former Ambassador to the U.S. and UN (54 years old). Guterres is an estranged member of Fretilin who allied himself with Gusmao's CNRT party in the 2007 parliamentary elections. He led the "Mudansa" (reform) element within Fretilin and unsuccessfully challenged Alkatiri for party leadership in 2006. Guterres could return to lead Fretilin, still the best-organized and most national of Timor's parties, should Alkatiri decide or be forced to step aside.

-- Aniceto Guterres, head of Fretilin's parliamentary caucus (42

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years old). Guterres is spearheading Fretilin's preparations for the upcoming local elections. He chaired the CAVR commission that investigated crimes during the Indonesian occupation and is a human rights lawyer by profession. Guterres is a possible replacement for Alkatiri as leader of Fretilin.

Building Institutions Across the Board

¶13. (SBU) Timor-Leste's basic governance institutions are still works in progress. The country needs but still lacks police that can combat criminal activity, serve the people and keep domestic order; a professional, disciplined military that carries out a well-defined national security mission; political parties that institutionalize the peaceful transfer of power; a justice system that credibly and expeditiously punishes the guilty and resolves disputes; an educational system that delivers basic literacy and numeracy; and a health system that reduces infant mortality and extends life expectancy.

Reaping Real Benefit from Petroleum Revenue

¶14. (SBU) Timor-Leste's known oil and gas resources provide a one-generation window to build the country. The total value of reserves is estimated to be between \$14 billion and \$20 billion, to be expended on a sustainable basis if the government continues to abide by the strictures of the Petroleum Fund. To

date, petroleum revenue has financed a massive ten-fold increase in government spending. Recurrent expenditures such as wages and salaries still make up the majority of the budget, but the share allotted to capital expenditure and development projects is growing. Among other tasks the increased revenue enabled Timor to buy its way out of two sources of instability by offering one-time buyouts to the petitioners and resettlement bonuses to IDPs. Additionally, it has also enabled the government to establish a very popular welfare system for the elderly, veterans, and the infirm; to make an enormous purchase of rice to guard against food riots that occurred in the past; and to afford a large number of overseas scholarship programs for Timorese students.

¶15. (SBU) Timor-Leste must generate substantial labor-intensive activities to soak up a pool of unemployed that is poised to grow massively in the years ahead. Close to half the population is under the age of 15 and the birth rate is among the highest in the world. Unemployed youths have fueled Dili's street violence and unrest in the past, drawn to the city without the job creation needed to sustain them. Sectors such as coffee, processed foods, handicrafts and tourism offer potential for growth but even in optimistic scenarios the likelihood of substantial manufacturing activity is low. Government investment in badly-needed infrastructure projects offers the best opportunity to create the employment that is needed to keep Timor-Leste's coming generation gainfully occupied. There is broad support to bring a gas pipeline to Timor-Leste as a future offshore field is exploited. While proponents of the pipeline

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hope it will provide the basis for a small petro-chemical industry, there is considerable skepticism regarding its cost and viability.

U.S. Strategy

¶16. (SBU) The United States has a unique opportunity to play a positive role in Timor-Leste's continued development as a country. We do not have the same historical baggage as Timor-Leste's other major international partners, such as Australia, Indonesia, Portugal and the United Nations. It is easier for the Timorese to accept us as an honest broker supporting the development of Timorese democratic institutions. Our fundamental interest here is to extend the period of stability that began 18 months ago and ensure that this is merely the beginning of a new, more positive phase of consolidation, stability and development.

¶17. (SBU) To achieve this, the United States will continue to engage and assist the Timorese pursue their priority goals, including developing and strengthening essential institutions. Our development assistance strategy focuses on accelerating economic growth, strengthening good governance, especially security sector reform, and improving health. U.S. programs have produced significant achievements in coffee production, land and property rights, private sector development, elections, independent media, and public health, results that help to plug yawning gaps that threaten the foundation of Timor-Leste's future success. Anti-corruption and judicial assistance will be crucial in the years ahead to ensure that the rule of law takes hold and that the public's faith in its political institutions is not squandered. Growing military-to-military engagement will help to professionalize Timor-Leste's armed forces and keep them

from being a spoiler on peace and stability issues. The return of the Peace Corps would be a dramatic sign of support of Timor-Leste at the grassroots level, one which would have great resonance in the country from the top of the country's political leadership on down. Ten years after the start of Timor-Leste's road to independence there is much left to do -- and much that the United States can do -- to ensure that the next ten years achieve the promise that all friends of Timor-Leste hope and believe is possible.

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